cc: Richard Perle, Bob Komer, Joe Fitchett, Paul Friedrich

France: It Can't Postpone a Reckoning Forever

Paris

The French government of the left has taken some austerity measures since its second devaluation in mid-June but these steps have at best stopped the franc's degradation process—not reversed it.

The government has had to face two problems. There are the unresolved difficulties created by the quasi-permanent

Europe

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weakness of the French franc within the European Monetary System. And there is the goal of keeping the buying power of workers rising through the distribution of social benefits despite a stagnating economy.

The government, which is waiting with discomfort for the municipal elections in March, is indulging in the universal panacea: It has heavily increased its borrowing abroad and intends to keep on this same path.

During Raymond Barre's tenure as finance minister in 1979-80, France borrowed $2.5 billion to $4 billion a year. In 1982 this figure was raised to $7 billion to $8 billion. France was the biggest borrower in world markets in 1982, when it raised over $20 billion and pushed its external debt to more than $50 billion.

Of the $20 billion, roughly $9 billion went to financing loans the French are themselves extending to foreign debtors. Some $4.5 billion has been used to pay the principal and interest on France's external debt. What remains has been used to finance the current balance of payments deficit of about $15 billion, up fourfold from 1980. (In addition to the increase in external debts, about $6 billior

So far the credit ratings of the French Republic and the entities that revolve around it have remained on the whole quite good. There is no doubt that there is large scope for further borrowing but there are also growing signs of both financial and political unease that show the government will not be in a position to pursue such a policy of postponement for very long without important negative consequences.

For one thing, the franc remains very fragile in spite of being temporarily propped up by the huge inflow of funds through the borrowing. Last week, after much hesitation, the government finally lowered by a full point the interest rate charged French business borrowers on some credits granted at concessionary terms. About half of the medium- and long-term credits extended in the French economy bear subsidized interest rates. Simultaneously the banks, acting on the injunction of Economy and Finance Minister Jacques Delors, cut a quarter point off the prime rate, to 12.25%. The authorities would have liked to lower the money market rate, which is now four points above the Eurodollar rate, but cannot do so without endangering the franc.

There is an obstinate minority in the Socialist parties pleading that France should isolate itself by abolishing the money market and replacing it with authoritarian allocation of reserves to the commercial

such a radical move. But with unemployment above two million (8.7%), it would be politically very difficult to raise interest rates to their former level. The views of the radicals could, in different circumstances, yet be heard.

Heavy indebtedness can also easily be interpreted as a threat to the sacred idea of "national independence" and fuel the trend toward protectionism. A rather ridiculous illustration of this was the decision to clear video recorders (most of them Japanese) through customs in Poitiers, a city deep in the country far from a harbor.

The reason France is obliged to raise money abroad is that domestic savings, which have fallen to a historically low level, cannot match the financial requirements of the government, the social security system and the productive sector. The central government deficit should not exceed 3% of GNP this year, but tax receipts have been estimated on the quite optimistic assumption of 2% economic growth. The main burden of the social security system will come from one of the most unwise decisions taken by the left coalition—setting the full-benefit retirement age at 60 instead of the previous 65.

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The other most unreasonable decisions have been the nationalizations and the reducing of the legal working time. The result of the reduced hours will be that unemployed people will be replaced by prematurely retired people and there will be

Two-thirds of the public sector deficit i: financed indirectly by the monetization o the debt, a permanent source of inflation i France. The government has sought t limit price and wage increases to 8% : year through a combination of controls an jawboning. A decision had even been an nounced to abolish indexation of wages but the Communist minister in charge o the public sector just ignored it. He als restored, in a slightly moderated way, ir dexation for the civil servants, who enjo perfect job stability. The outcome is tha unions are refusing to sign contracts tha include a repudiation of indexation.

The important fact is that Presider Mitterrand did not veto the Communis minister's decision. The question is raise about the influence of the Communis Party in economic (and other) affair which appears greater today then it wa generally assumed a few months ago.

The second point is that the governme is speaking in terms of an ambitious "i dustrial policy," but the much increase appropriations for the enlarged nationa ized sector will just pay for the deficits those nationalized industries, which a sometimes prevented from laying off u needed personnel. (According to figures r leased yesterday, there is a $3.6 billion de icit for nationalized industries since 1981 Little money is likely to be left over for nancing fresh investment.

On top of that, nationalized industri have not yet overcome the trauma of bei taken over. In some nationalized bank managers face the problem of "demotiv tion" among the professionals. The gover ment is becoming conscious of this ph nomenon, a fact of utmost importance b cause this consciousness is a warni against pushing too far for a Socialist pr gram of income redistribution, the resu of which would be to "demotivate" larger part of the working population.

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